

Generally, medical tools, devices and equipment used for diagnostic, rehabilitative and treatment purposes do not qualify for the reduced rate of tax for medical appliances as such items, while being used for the treatment of patients, are not directly substituting for a malfunctioning part of the body. See 86 Ill. Adm. Code 130.310(c). (This is a GIL.)

November 19, 2001

Dear Xxxxx:

This is in response to your letter dated August 15, 2001. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120 subsections (b) and (c), which can be found at <http://www.revenue.state.il.us/legalinformation/regs/part1200>.

In your letter you stated and made inquiry as follows:

We would like the Illinois Department of Revenue's help in determining whether the products we sell to customers in Illinois are exempt from sales tax. We would like to request that the response be sent to us in writing.

Products:

NAME sells Radio frequency (RF) Generators and Catheters to hospitals, surgical centers and doctors. The RF generator may be classified as capital medical equipment and the catheter may be classified as a disposable medical device/instrument. These products are used to perform the Closure® procedure on patients with Venous disease and varicose veins.

Closure® Procedure:

The Closure® procedure is an outpatient (day surgery) treatment performed in doctor's offices, surgical centers and hospitals. This surgical procedure uses a very small catheter and radio frequency energy to occlude or seal shut the saphenous vein. Local or regional anesthesia is used to numb the treatment area. A physician typically makes a single incision near the knee and the catheter is inserted into the vein through the small opening, using a single needle stick. The catheter delivers bipolar radio frequency (RF) energy directly into the vein wall. The passage of heat through the vein wall causes resistive heating, which shrinks the vessel. The Closure® procedure is intended for endovascular coagulation of blood vessels in patients with superficial venous reflux.

Product Use:

The RF generator is used to generate a radio frequency energy, which gets delivered by the catheter to the vein.

The primary function of the catheter is to deliver the bipolar radio frequency energy from the generator into the patient's vein, which causes the vein to heat, collapse and seal shut. Along with the radio frequency energy, the catheter also delivers the prescription drug heparin into the vein in each surgical case. Heparin acts as an anticoagulation agent during the Closure® procedure.

Customers:

NAME sells to hospitals, clinics, surgical centers and doctors who use our products to perform surgery on patients. Since our products are used in a surgical procedure that can only be performed by physicians, the equipment and devices do not get resold to patients. Even though they are used on patients, the end customer is the hospital or the doctor.

Some of these customers are a tax-exempt or not-for profit entity, please advise us as to what would be acceptable proof that we need from them to relieve us from liability.

Taxability on various Purchase Options:

Besides purchasing the RF generators directly, our customers also have two other options. Please advise NAME on the first issue only in the event that the IL Department of Revenue determines that the catheters are non-taxable but the generator is taxable.

The first option is that the customer commits to purchase a designated number of catheters during a specified time frame at a package price including the RF generator. At the completion of the agreement, title to the generator passes to the customer.

In this instant, customers may record the RF generator as a free product but on NAME records the transaction is a sale. In this case who is liable for the tax?

The second option is that the customer rents the RF generator for a monthly rental fee. In this case, should the monthly rental fee on the RF generator have sales tax assessed?

Thank you for your cooperation in helping us determine the taxability of our products.

All gross receipts from the sale of tangible personal property are subject to the Retailers' Occupation Tax unless specifically exempted. A specific exemption from the regular sales tax rate of 6.25% is allowed for medicines and medical appliances. Medicines and medical appliances are taxed at the lower rate of 1%, plus applicable local taxes. See the enclosed copy of 86 Ill. Adm. Code 130.310.

A medical appliance is defined as an item intended by its manufacturer for use in directly substituting for a malfunctioning part of the body. Examples of items that qualify are artificial limbs, dental prostheses and orthodontic braces, crutches and orthopedic braces, wheelchairs, heart pacemakers, and dialysis machines. Corrective medical appliances such as hearing aids, eyeglasses and contact lenses are also examples of qualifying items. Generally, medical tools, devices and equipment used for diagnostic, rehabilitative and treatment purposes do not qualify for the reduced rate of tax for medical appliances as such items, while being used for the treatment of patients, are not directly substituting for a malfunctioning part of the body. See Section 130.310(c)(2).

From the limited information provided in your letter, the Radio frequency (RF) generators and catheters used for the Closure procedure you describe do not appear to be medical appliances directly substituting for a malfunctioning part of the body. Rather, these instruments are used during a surgical procedure to assist the patient's vein in closing and to administer a drug as part of the treatment for superficial venous reflux. Therefore, sales of such products for use in Illinois are subject to the regular 6.25% sales tax rate, plus applicable local taxes.

When selling your products to customers that claim a tax-exempt status, please be aware that only institutions, associations and organizations that make application to the Department and are determined to be organized and operated for exclusively religious, educational or charitable purposes are exempt from Use Tax when purchasing tangible personal property for use in the furtherance of organizational purposes. See the enclosed copies of 86 Ill. Adm. Code 130.2005 and 130.2007. The Department issues a tax exemption identification number ("E" number) to organizations determined to be organized for exclusively religious, educational or charitable purposes. Retailers will not incur Retailers' Occupation Tax on sales to such organizations where a valid E number is presented to the retailer.

With regards to the rental of the RF generators, please find enclosed a copy of 86 Ill. Adm. Code 130.2010, the Department's regulation covering taxation of leases. Taxation of leases depends upon whether the lease is a "true lease" or a lease that is actually a conditional sales contract.

Rental receipts from renting tangible personal property under a true lease agreement are not subject to tax. A lessor of property under a true lease is deemed the end user of the leased property and incurs Use Tax liability on his cost price of the property when the property is purchased for lease. The Use Tax incurred by a lessor may not be passed on to a lessee as a tax. See Section 130.2010(b).

A true lease is a lease that does not have a buy out provision at the close of the lease, and therefore the product leased is returned to and remains the property of the lessor at the end of the lease. If a buy out provision does exist, it must be a fair market value buy out option in order to maintain the character of a true lease.

Where a lessor of tangible personal property actually transfers the property to the lessee at the end of the lease for a nominal purchase option amount, or for no consideration the lessor has made a conditional sale of the property and all payments received by the lessor are subject to Retailers' Occupation Tax. See Section 130.2010(a).

Please be aware that a recent legislative change has made available an exemption from Retailers' Occupation Tax for sales to lessors of certain tangible personal property leased to exempt hospitals. The availability of this exemption ended on December 31, 2000, however, with passage of Public Act 92-227, the exemption again became available, effective August 2, 2001. The sale of equipment used in the diagnosis, analysis, or treatment of hospital patients to lessors of such equipment and leased to exempt hospitals is exempt from sales tax. In order for the sale to be exempt, however, all equipment must be purchased for lease to a tax exempt hospital under a lease of a period of one year or more and having been executed or in effect at the time of purchase. Additionally, the hospital lessee must have an active tax exemption identification number issued to the hospital by the Department. See the enclosed 86 Ill. Adm. Code Section 130.2011, the Department's regulation explaining this exemption, for further information. Please note, however, that this regulation is currently in the process of being amended, and therefore, does not reflect the new effective date for tax exempt purchases of such equipment by persons leasing to exempt hospitals.

I hope this information has been helpful. The Department of Revenue maintains a website, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales and use tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b).

Sincerely,

Dana Deen Kinion
Associate Counsel

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Enc.